

## Pinduoduo (PDD US)

### Robust growth momentum

- Robust revenue growth momentum supported by business improvement
- Ongoing investment in business expansion and overseas regulatory risks are major swing factors
- Maintain **BUY** with a revised TP of US\$ 200

**Strong growth supported by ongoing business improvement.** Pinduoduo reported robust revenue growth of 131% YoY in 1Q24. In particular, driven by the continuing development of Temu, transaction service revenue rose by 327% YoY and accounted for 51% of total revenue. In our view, such strong growth momentum is supported by operational initiatives such as strengthening logistics services to remote rural areas and providing a more flexible business model to Temu merchants. We believe these initiatives help the company strengthen customer and merchant relationships and its value-to-money product offerings. Looking forward, we expect revenue to increase at 43% CAGR in 2023-25E on business improvement and international expansion.

**Swing factors.** Despite its robust revenue growth, Temu is still in the development phase, which requires continuous investment in marketing, international logistics infrastructure, and other aspects to support future business growth- these could reduce margin visibility ahead. In addition, regulatory risk regarding overseas businesses remains an ongoing concern, partly mitigated by the company's plan to step up compliance monitoring on merchants' products and Temu's ongoing diversification from US market.

**Maintain BUY.** We maintain our **BUY** rating with a revised TP of US\$ 200 given Pinduoduo's strong growth momentum. Our TP implies 17.3x 2025E core P/E. On the flip side, overseas regulatory risk is partly mitigated by the counter's undemanding valuation.

#### Results and Valuation

FY end Dec 31	2022A	2023A	2024E	2025E
Revenue (RMB mn)	130,558	247,639	385,838	508,988
Chg (% YoY)	39.0	89.7	55.8	31.9
Net profit (RMB mn)	31,538	60,027	85,877	115,669
Chg (% YoY)	306.0	90.3	43.1	34.7
Core net profit (RMB mn)	39,529	67,899	101,810	136,528
Chg (% YoY)	185.8	71.8	49.9	34.1
Earnings per ADS (RMB)	21.9	41.1	58.8	79.2
Chg (% YoY)	302.6	87.8	43.1	34.7
Core earnings per ADS	27.4	46.5	69.7	93.5
Chg (% YoY)	183.4	69.5	49.9	34.1
Core P/E (x)	39.7	23.4	15.6	11.6
P/S (x)	12.0	6.4	4.1	3.1
ROAE (%)	32.7	39.4	36.1	32.4
ROAA (%)	15.7	20.5	20.2	20.5

Note: 1ADS=4 ordinary shares

Source (s): Bloomberg, ABCI Securities estimates

## Company Report

### May 31, 2024

Rating: **BUY**  
 TP: US\$ 200

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Price	US\$ 151.2
Est. share price return	32.3%
Est. dividend yield	NA
Est. total return	32.3%
Last Rating & TP	BUY, US\$185
Previous Report Date	Mar 22, 2024

Source(s): Bloomberg, ABCI Securities estimates

#### Key Data

52Wk H/L (US\$ )	164.7/62.5
Outstanding shares (mn)	5,509
Market cap (US\$ mn)	208,240
3-mth avg daily turnover (US\$ mn)	1,573
Major shareholder(s)	
Zheng Huang	25.7%

Source(s): Bloomberg, Company

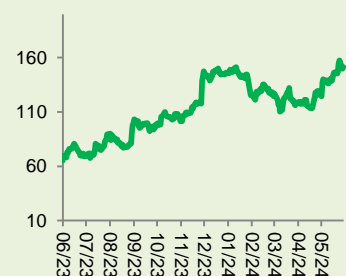
#### Share Performance (%)

	Absolute	Relative*
1-mth	20.8	18.4
3-mth	21.5	11.3
6-mth	2.6	-4.1

\*Relative to MXCN

Source(s): Bloomberg, ABCI Securities

#### Share performance (US\$)



Source(s): Bloomberg, ABCI Securities

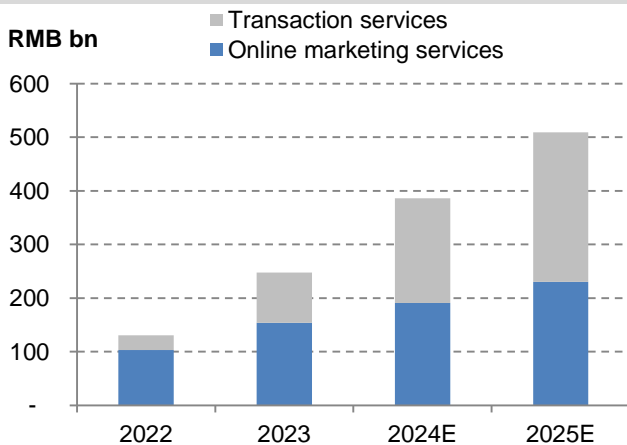
## Financial outlook

We expect revenue to increase at 43% CAGR in 2023-25E, primarily driven by improving monetization via providing more value-added services to merchants and rising contributions from emerging businesses, including Temu.

**Online marketing service:** We expect online marketing service, which mainly includes performance-based marketing services, such as search ranking, recommendation feeds, among others, to increase at 22% CAGR in 2023-25E, driven by improved monetization through better service offerings and merchant stickiness.

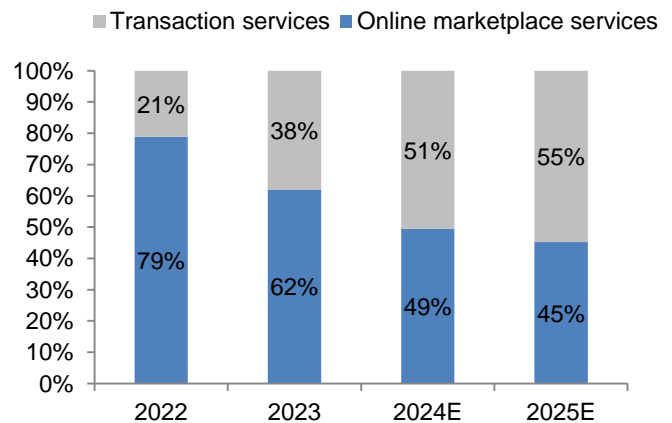
**Transaction services:** We expect transaction services revenue to increase at 72% CAGR in 2023-25E on growing contributions from emerging businesses. As a result, we expect the segment's contribution to total revenue to increase from 38% in 2023 to 55% in 2025E. Specifically, Temu, which takes on a value-to-money market position, has been gaining popularity amid overseas expansion. We expect its overall revenue contribution to Pinduoduo to be in the 40s range by 2025E.

**Exhibit 1: Revenue trend**



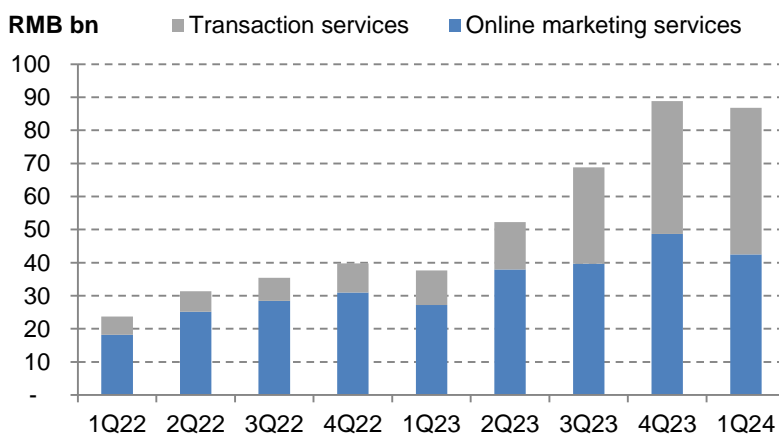
Source(s): Company, ABCI Securities estimates

**Exhibit 2: Revenue mix**



Source(s): Company, ABCI Securities estimates

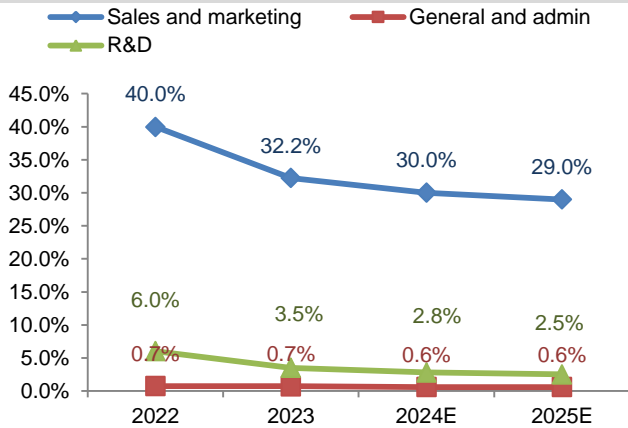
**Exhibit 3: Segment revenue trend**



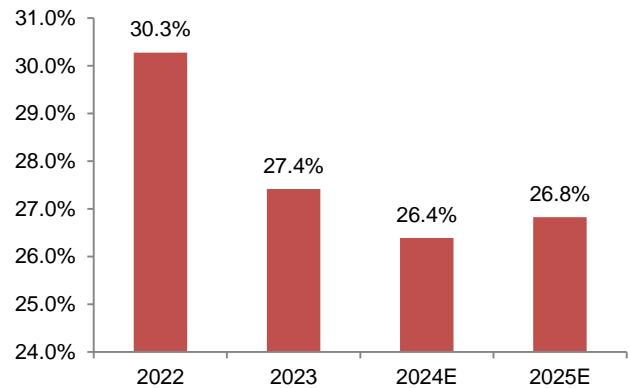
Source(s): Company, ABCI Securities

Despite strong revenue growth, Temu remains in the development stage, necessitating ongoing investment in marketing and other consumer incentives to maintain its value-for-money market position. In addition, investments in international logistics infrastructure will be needed to support its global expansion. In our view, this could potentially lead to margin volatility in the future.

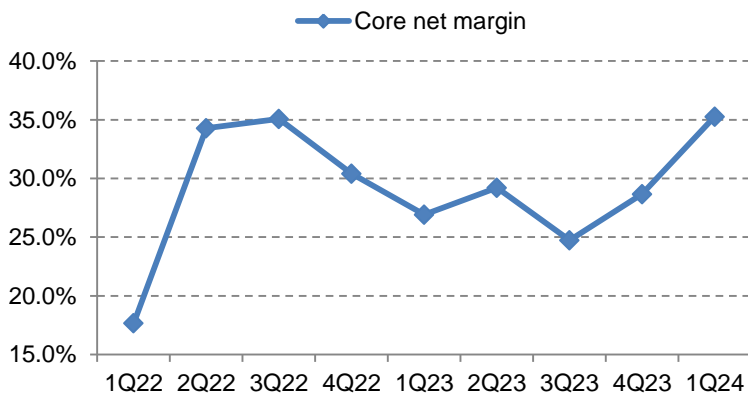
Overall, we expect non-GAAP core net profit to expand at 42% CAGR in 2023-25E, with core net margin moderating to 26.8% in 2025E.

**Exhibit 4: Non-GAAP cost trend (% of revenue)**


Source(s): Company, ABCI Securities estimates  
 Note: Excl. impacts of share-based compensation and other non-operating items

**Exhibit 5: Core net margin**


Source(s): Company, ABCI Securities estimates

**Exhibit 6: Core net margin trend**


Source(s): Company, ABCI Securities

**Exhibit 7: Financial forecast changes**

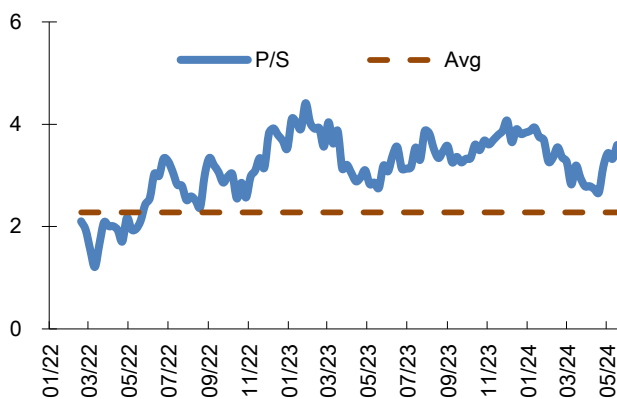
	2024E			2025E			Comment
	old	new	Diff	old	new	Diff	
Revenues	356,526	385,838	8%	452,710	508,988	12%	Strong growth in overseas business
Core profit	85,776	101,810	19%	111,000	136,528	23%	Operating leverage

Source(s): ABCI Securities estimates

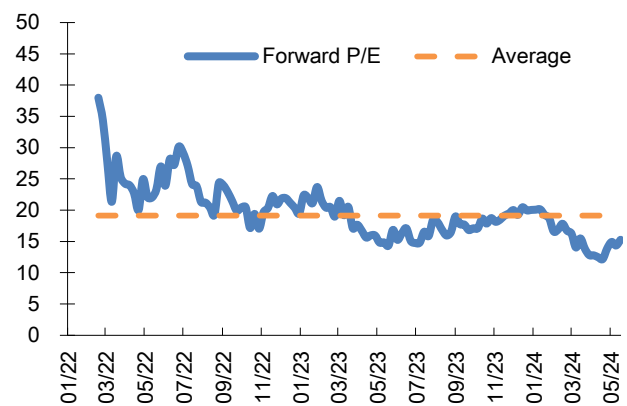
## Valuation and TP

We maintain our **BUY** rating on the counter with a revised TP of US\$ 200 to reflect Pinduoduo's robust momentum. Our TP implies 15.4x 2025E core P/E, which we believe is undemanding.

On the flip side, regulatory risk regarding overseas businesses remains an ongoing concern, partly mitigated by the company's plan to step up compliance monitoring on merchants' products and Temu's ongoing diversification from US market. In addition, the possibility of delisting in the US remains, and the company is one of the few major online platforms that does not hold a dual listing status. Having said that, we believe these risks have been priced into the counter's undemanding valuation.

**Exhibit 8: P/S trend**


Source(s): Bloomberg, ABCI Securities

**Exhibit 9: Forward P/E trend**


Source(s): Bloomberg, ABCI Securities

**Exhibit 10: TP changes (US\$ per share)**

Old	New	Remark
185	200	DCF with revised financial forecast, 12% WACC (unchanged), and 3% terminal growth rate (unchanged)

Source(s): ABCI Securities estimates



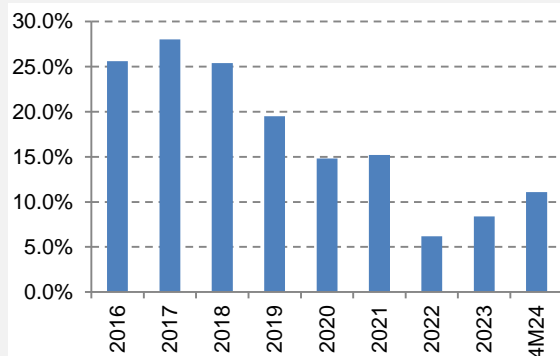
## Company profile

Business
<ul style="list-style-type: none"> <li>Major e-commerce platform in China with an <b>estimated market share at the mid-20s level</b></li> <li>Platform-based business model, which generally does not bear inventories</li> <li><b>Rapid growth in recent years</b> despite a relatively short operating history since 2015</li> <li>Rising popularity driven by its <b>innovative business model</b> that provides buyers with value-for-money products and interactive shopping experiences. For example, it offers various "mini-games" for users to earn coupons</li> <li>"RMB 10bn subsidy" has been its major marketing program in recent years to reinforce its <b>"value-for-money" proposition</b></li> <li>Annual active buyers estimated to be over 900mn, similar to Alibaba (9988 HK/BABA US)</li> <li>Estimated GMV per buyer is around RMB 3-4K, vs. about RMB 9-10K for Alibaba, illustrating its focus on the value-for-money segment</li> <li>Strategic partnership with Weixin to leverage its traffic</li> <li><b>Strategic investments in agriculture</b> in recent years</li> <li><b>Launched Temu for the international market</b> in 3Q22 with growing popularity globally</li> </ul>
Financials
<ul style="list-style-type: none"> <li>High gross margin over 60% thanks to platform-based business model, but a changing business mix towards emerging businesses may shave margins</li> <li><b>Marketing expenses has been a major cost item</b> and swing factor for profitability, given its value-for-money proposition</li> <li><b>Strategic shift from marketing to R&amp;D</b> and emphasis on quality growth has led to more controlled marketing expenses in recent quarters, thus improving overall profitability</li> <li>Achieved break-even since 2Q21 with core net margin rising to 25%-35% range in recent quarters</li> <li><b>Swing factors for future profitability</b> include potential increase in customer subsidies to compete in the market as well as Temu's profitability</li> <li><b>Strong balance sheet</b> with RMB 242bn cash and short-term investment against RMB 5.2bn convertible bonds in Mar 2024</li> </ul>
Management and shareholder
<ul style="list-style-type: none"> <li>Largest shareholder and co-founder Zheng Huang <b>stepped down from his management role</b> as Chairman/member of the board of directors in Mar 2021. He also gave up his 1:10 super-voting power and entrusted his voting rights to the board. CEO Lei Chen was appointed as the new Chairman.</li> <li><b>PDD partnership:</b> PDD partnership is entitled to appoint executive directors and nominate and recommend the CEO</li> <li><b>No dividend record</b> since listing</li> <li><b>US delisting risk</b> arising from tightened regulatory requirement</li> <li><b>Strategic shareholder</b>, a major online platform in China, holds about a c 14.3% stake</li> </ul>
Corporate governance/information disclosure
<ul style="list-style-type: none"> <li>Like other major e-commerce platforms, the company has ceased disclosing some operational metrics such as GMV/users in recent years</li> <li><b>Google reportedly suspended the Pinduoduo app in Mar 2023</b> due to information security concerns, while Pinduoduo has rejected its claim</li> <li>Temu is facing <b>increasing regulatory scrutiny overseas</b> over its business practices, handling of user data, etc.</li> <li>Various ESG initiatives in recent years</li> </ul>

## Industry profile: Online shopping

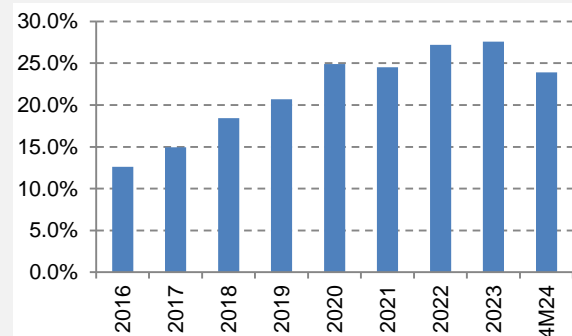
- **China's online sales growth has turned steadier** after years of development. According to NBS, online sales of physical goods grew 8.4% YoY in 2023. In 4M24, online sales growth of physical goods rebounded to 11.1% YoY, mainly due to low base. By product category, online sales of food products, groceries, and apparel rose 19.2%, 9.8%, and 10.5% in 4M24.
- **Online shopping penetration rate was generally in an uptrend** in recent years, indicating an ongoing consumption shift from offline to online
- **Live-streaming e-commerce** has been fast growing in recent years. In 9M23, live-streaming e-commerce sales rose by 60.6% YoY and accounted for 18.3% of total online sales, according to Ministry of Commerce. Short video platforms such as Douyin and Kuaishou (1024 HK) are major players in this emerging segment, leading to competitive pressure to traditional e-commerce platforms. On the other hand, Alibaba has been actively developing live-streaming business to defend its market position
- Major e-commerce platforms are **increasing their sales and marketing efforts** by raising user incentives and price subsidies. In our view, **online shoppers have turned more price-sensitive** in past years due to the pandemic and moderating economic development, prompting e-commerce platforms to enhance price competitiveness
- In terms of market share, we estimate that Alibaba is still the largest e-commerce platform with a mid-40s market share, vs. Pinduoduo (mid-20s), Platform A (low-20s), Douyin (high-single-digit), and Kuaishou (mid-single-digit)
- Over the past few years, **Pinduoduo and short-video platforms (Douyin and Kuaishou) are gaining market shares**. Common features of these platforms: 1) Product offers have low prices; 2) More interactive features (social e-commerce, live streaming, etc.) than traditional search-based e-commerce format
- Selected platforms such as Pinduoduo and Shein are actively developing **cross-border e-commerce** and have gained growing traction in various overseas markets

**Exhibit 11: Online sales growth of physical goods (YoY)**



Source(s): NBS, ABCI Securities

**Exhibit 12: Online shopping penetration rate**



Source(s): NBS, ABCI Securities



## Financial forecast

### Consolidated income statement (2022A-2025E)

FY Ended Dec 31 (RMB mn)	2022A	2023A	2024E	2025E
<b>Total revenue</b>	<b>130,558</b>	<b>247,639</b>	<b>385,838</b>	<b>508,988</b>
Cost of sales	(31,462)	(91,724)	(146,906)	(194,813)
<b>Gross profit</b>	<b>99,095</b>	<b>155,916</b>	<b>238,932</b>	<b>314,175</b>
Sales and marketing	(54,344)	(82,189)	(120,884)	(154,378)
General and admin	(3,965)	(4,076)	(7,306)	(9,638)
R&D	(10,385)	(10,952)	(15,825)	(19,349)
<b>Operating Profits</b>	<b>30,402</b>	<b>58,698</b>	<b>94,916</b>	<b>130,810</b>
Interest income	3,997	10,238	7,500	7,500
Interest expenses	(52)	(44)	(100)	(100)
Fx gain	(150)	36	0	0
Others, net	2,221	2,953	1,000	1,000
Share of results of investee	(155)	(5)	150	150
<b>PBT</b>	<b>36,264</b>	<b>71,876</b>	<b>103,466</b>	<b>139,360</b>
Tax	(4,726)	(11,849)	(17,589)	(23,691)
<b>PAT</b>	<b>31,538</b>	<b>60,027</b>	<b>85,877</b>	<b>115,669</b>
Minority interests	0	0	0	0
<b>Net profit</b>	<b>31,538</b>	<b>60,027</b>	<b>85,877</b>	<b>115,669</b>
Share-based compensation	7,718	7,079	15,434	20,360
Other non-core items	273	794	500	500
<b>Core net profit</b>	<b>39,529</b>	<b>67,899</b>	<b>101,810</b>	<b>136,528</b>
<b>Growth</b>				
Total revenue (%)	39.0	89.7	55.8	31.9
Gross Profit (%)	59.2	57.3	53.2	31.5
Operating Profit (%)	340.8	93.1	61.7	37.8
Net profit (%)	306.0	90.3	43.1	34.7
Non-GAAP net profit (%)	185.8	71.8	49.9	34.1
<b>Operating performance</b>				
Operating margin (%)	23.3	23.7	24.6	25.7
Net margin (%)	24.2	24.2	22.3	22.7
Core net margin (%)	30.3	27.4	26.4	26.8
ROAE (%)	32.7	39.4	36.1	32.4
ROAA (%)	15.7	20.5	20.2	20.5

Note: Individual items may vary from reported figures due to rounding /definition differences

Source(s): the Group, ABCI Securities estimates



Consolidated balance sheet (2022A-2025E)

As of Dec 31 (RMB mn)	2022A	2023A	2024E	2025E
Fixed assets	1,045	980	2,980	4,980
Intangible assets	134	21	22	22
Financial investments	16,862	47,951	57,951	67,951
Other non-current assets	2,461	4,376	4,390	4,390
<b>Total non-current assets</b>	<b>20,502</b>	<b>53,328</b>	<b>65,342</b>	<b>77,342</b>
Cash & equivalents	34,326	59,794	183,314	289,621
Restricted cash	57,974	61,985	68,184	68,184
Short-term investments	115,113	157,415	167,415	177,415
Account receivables	588	3,914	4,110	4,110
Other current assets	8,617	11,641	12,012	12,012
<b>Total current assets</b>	<b>216,618</b>	<b>294,750</b>	<b>435,036</b>	<b>551,342</b>
<b>Total assets</b>	<b>237,119</b>	<b>348,078</b>	<b>500,378</b>	<b>628,684</b>
Payable to merchants	63,317	74,997	116,442	114,721
Merchant deposit	15,058	16,879	26,689	25,919
Convertible bonds and borrowings	13,886	649	5,231	0
Other current liabilities	24,628	60,376	60,627	60,627
<b>Total current liabilities</b>	<b>116,889</b>	<b>152,901</b>	<b>208,989</b>	<b>201,267</b>
Convertible bonds	1,576	5,232	-	-
Other non-current liabilities	884	2,704	2,836	2,836
<b>Total non-current liabilities</b>	<b>2,460</b>	<b>7,936</b>	<b>2,836</b>	<b>2,836</b>
<b>Total liabilities</b>	<b>119,349</b>	<b>160,836</b>	<b>211,826</b>	<b>204,104</b>
Equity attributable to shareholders	117,771	187,242	288,552	424,580
Non-controlling interests	-	-	-	-
<b>Total equity</b>	<b>117,771</b>	<b>187,242</b>	<b>288,552</b>	<b>424,580</b>

Note: Individual items may vary from reported figures due to rounding /definition differences

Source(s): the Group, ABCI Securities estimates

Consolidated cash flows (2022A-2025E)

As of Dec 31 (RMB mn)	2022A	2023A	2024E	2025E
Net income	31,538	60,027	85,877	115,669
Depreciation and amortization	2,224	786	2,000	2,000
Other non-cash adjustments	7,323	6,894	15,434	20,360
Change in working capital	7,423	26,456	44,858	(2,491)
<b>Operating cash flow</b>	<b>48,508</b>	<b>94,163</b>	<b>148,168</b>	<b>135,537</b>
Acquisition of fixed asset	(636)	(584)	(4,000)	(4,000)
Net purchase of investments	(21,090)	(54,977)	(20,000)	(20,000)
Other investment cash flow	(636)	130	-	-
<b>Investing cash flow</b>	<b>(22,362)</b>	<b>(55,431)</b>	<b>(24,000)</b>	<b>(24,000)</b>
<b>Financing cash flow</b>	<b>10</b>	<b>(8,961)</b>	<b>(649)</b>	<b>(5,231)</b>
Fx effect	100	(291)	-	-
<b>Net cash flow</b>	<b>26,256</b>	<b>29,480</b>	<b>123,520</b>	<b>106,306</b>

Individual items may vary from reported figures due to rounding /definition differences

Source(s): the Group, ABCI Securities estimates





## Risk factors

### Market competition

The ecommerce industry is highly competitive, with companies contending on commission rate, promotion discount, brand advertising, technological investment, and more.

### Slowdown in ecommerce consumption

As the industry is dependent on consumer spending, any significant slowdown of consumption in China would hamper the company's performance. In the long term, we believe consumption growth in domestic market would converge with income growth, which is usually in line with GDP growth.

### US regulatory risk

Pinduoduo's Temu has a growing operation in the US, and is subject to US regulatory risk given the rising geopolitical tension between China and the US.

### Non-GAAP financials

Ecommerce platforms generally disclosed the non-GAAP financial metrics, such as the non-GAAP net profit, to supplement its GAAP financial measures. Historically, there were differences between its GAAP net profit and non-GAAP net profit due to inclusion of items such as share-based compensation and other non-core items in the former.

Among these items, share-based compensation expense is related to various factors, including price movement of ordinary shares, expected volatility, risk-free interest rate, etc.

While investors tend to exclude these items when performing analysis given their non-cash nature, we believe these non-GAAP financial measures should only serve as references.

### Dilution effect

In view of our expected TP of US\$200/ADS, we expect all outstanding CB (strike price US\$190.6) will be fully converted to ordinary shares or ADS before end-2025, leading to dilution effect. Potential increase in supply of free-float shares may induce share price volatility.

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### Definition of equity rating

Rating	Definition
Buy	Stock return rate $\geq$ Market return rate (7%)
Hold	- Market return rate (-7%) $\leq$ Stock return rate < Market return rate (+7%)
Sell	Stock return < - Market return (-7%)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months  
Market return rate: average market return rate since 2006 (HSI total return index 2005-23 averaged at 8.4%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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